

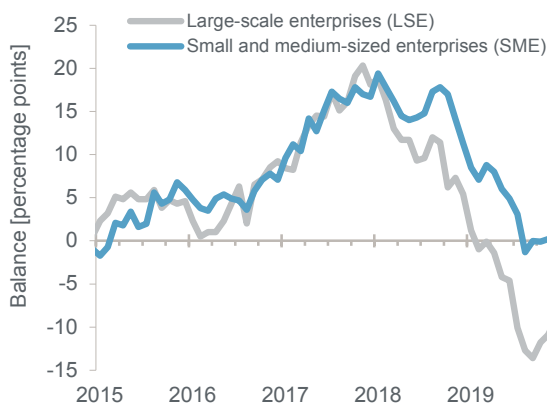
»» Despite minor bright spots at the end of the year, the road to a rebound is a long one

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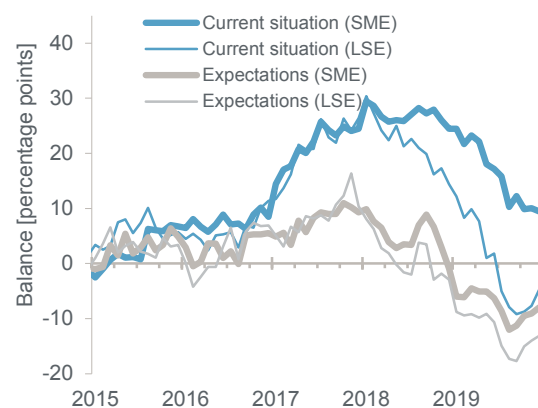
- SME business sentiment is up slightly on the previous month
- Expectations have improved, but situation assessments have deteriorated
- Business climate among large enterprises is emerging from a multi-year trough
- Economy starts new year with little impetus

KfW-ifo business climate



Source: KfW Research, ifo Institute

KfW-ifo climate components



Year has ended on a more or less conciliatory note

There is still no real improvement in the SME business climate. SME business sentiment rose by 0.3 points in December, bringing an economically difficult year to a more or less conciliatory end. At 0.5 balance points, however, the key indicator of the KfW-ifo SME Barometer is now scraping along the zero line – which stands for the historic average and thus, demonstrates lack of economic direction – for the fifth consecutive month. The most recent minor sentiment improvement in the small and medium-sized enterprise sector is being carried exclusively by less pessimistic expectations:

- They improved by 1.1 points to now -8.0 balance points. Business expectations improved moderately across the entire fourth quarter on average as well, which at least raises hopes for a modest economic rebound from next spring.
- Assessments of the current business situation, on the other hand, dropped by 0.6 points to 9.5 balance points and were also down on average across the three months from October to December. This supports our expectation that real growth will hardly be above stagnation level in the fourth quarter of 2019, as it was in the third.

Sentiment among large enterprises is breaking out of the trough

As in previous months, the mood in large enterprises again improved more strongly than in the SME sector in December but was still on a much lower level. Specifically, their business situation assessments rose by 1.9 points to -9.0 balance points. With this third consecutive monthly increase, large enterprises are finally leaving behind the ten-year low to which their sentiment indicator dropped last September. While their business situation assessments rose by 3.0 points to -4.7 balance points, their expectations increased by 0.9 points to -13.1 balance points.

The economy remains split

SMEs and large enterprises largely agree on their cautious outlook on the future, as business expectations clearly remain negative in both company size classes irrespective of the most recent upward trends. By contrast, while assessments of the current business situation have converged somewhat, they remained very far apart in December as well, signalling that the economy remains divided for the time being. Positive situation assessments clearly prevail among the domestically oriented SMEs, while negative assessments predominate across export-oriented large firms.

A glimmer of hope for external trade

Even so, the first rays of hope are beginning to show that the divide between the robust domestic demand and the difficult external environment which has been observed for nearly two years now might at least begin to narrow in the course of the year 2020. Specifically, business situation assessments of large enterprises stabilised on average in the fourth quarter (+0.3 points on the previous quarter), while they dropped in the SME sector over the same period (-3.0 points on the previous quarter). This was primarily due to the noticeable improvements seen in those segments of the economy that are particularly exposed to global developments, namely large manufacturers (+3.4 points on the previous quarter) and wholesalers (+2.4 points on the previous quarter). But this positive trend in situation assessments was also visible among large service providers, which include many business-related services (+1.0 points on the previous quarter). This makes the external trade environment a bit less hostile, with the picture finally rounded off by manufacturers' export expectations which, after three consecutive monthly increases, in December climbed to the highest level since June (SMEs: +0.3 points to -10.4 balance points) and even since February (large enterprises: +4.7 points to -4.3 balance points). The partial agreement in the US-China trade dispute and the clear parliamentary majority that emerged from the election to the House of Commons in the United Kingdom, which now allows Brexit to take shape, appear to be having a positive impact.

The road to a genuine rebound is a long way off

The December finding of the KfW-ifo SME Barometer shows one thing above all: After the prolonged phase of international uncertainties, German enterprises appreciate even minor bright spots. We believe this is grounds for very cautious optimism, but not more. After all, the most recent de-escalation in the US-China trade dispute is by no means a solution to the fundamental conflict. And after the surprisingly clear election victory of the Conservative Party of Prime Minister Johnson, the United Kingdom will leave the EU on 31 January 2020 in an orderly fashion. In the immediately ensuing negotiations about the long-term relations, however, a range of deep rifts will likely open up again. According to the declared intention of the UK Government, the time window for overcoming these differences will be open for a mere eleven months, so the risk that Brexit can still end up without a deal is only being delayed to the end of 2020. Even if the very hard economic blows were just barely averted in the last minute, the road to a genuine upturn remains a long one. Overall, we see the most recent sentiment reflection provided by the KfW-ifo SME Barometer as confirmation of our current economic forecast of 0.5% for 2019 and 0.9% for 2020. However, the growth pickup in 2020 will be exclusively due to the additional output resulting from four additional working days. Adjusted for this calendar effect, Germany's gross domestic product will therefore grow by a mere 0.5% in 2020 and, thus, at the same weak pace as in 2019, for which the calendar effect is negligible.

KfW-ifo SME Barometer in figures

Balance [Percentage points]*		Month/Year							m-o-m	y-o-y	3m-o-3m
		Dez/18	Jul/19	Aug/19	Sep/19	Okt/19	Nov/19	Dez/19			
Business climate											
Manufacturing	SME	7.4	-10.8	-13.0	-13.0	-14.4	-13.0	-14.3	-1.3	-21.7	-1.6
	LSE	1.6	-23.1	-21.7	-21.2	-18.1	-20.3	-17.5	2.8	-19.1	3.4
Construction	SME	34.8	30.5	30.0	29.5	28.5	29.0	25.3	-3.7	-9.5	-2.4
	LSE	35.9	24.8	14.1	24.9	19.8	14.5	18.5	4.0	-17.4	-3.7
Retail trade	SME	11.0	11.2	13.1	9.8	8.5	12.3	12.5	0.2	1.5	-0.3
	LSE	-7.3	-1.1	5.5	0.4	-2.4	-4.2	-5.7	-1.5	1.6	-5.7
Wholesale trade	SME	7.0	-4.4	-7.9	-10.2	-9.3	-9.3	-11.0	-1.7	-18.0	-2.4
	LSE	5.0	-16.5	-10.7	-16.0	-14.7	-9.3	-11.9	-2.6	-16.9	2.4
Services	SME	8.7	4.5	-0.7	4.2	2.8	2.6	4.8	2.2	-3.9	0.7
	LSE	15.1	3.0	-5.6	-6.4	-4.6	-1.4	0.1	1.5	-15.0	1.0
Germany	SME	11.3	3.1	-1.3	0.0	-0.1	0.2	0.5	0.3	-10.8	-0.4
	LSE	5.4	-10.1	-12.7	-13.6	-11.8	-10.9	-9.0	1.9	-14.4	1.6
Current situation	SME	24.5	15.9	10.3	12.3	9.9	10.1	9.5	-0.6	-15.0	-3.0
	LSE	14.4	-5.0	-7.9	-9.2	-8.7	-7.7	-4.7	3.0	-19.1	0.3
Expectations	SME	-0.9	-8.6	-12.0	-11.3	-9.5	-9.1	-8.0	1.1	-7.1	1.8
	LSE	-2.9	-14.9	-17.3	-17.7	-15.0	-14.0	-13.1	0.9	-10.2	2.6
Employment expectations	SME	9.8	2.9	0.1	1.0	0.8	3.5	1.7	-1.8	-8.1	0.7
	LSE	15.7	-3.7	-1.4	-3.0	-2.3	-2.2	-4.4	-2.2	-20.1	-0.3
Sales price expectations	SME	14.9	2.4	3.0	0.9	3.1	3.3	4.7	1.4	-10.2	1.6
	LSE	12.8	-1.1	-1.0	-0.6	-0.4	1.9	2.7	0.8	-10.1	2.3
Export expectations of manufacturing	SME	-1.4	-12.2	-12.4	-14.1	-12.9	-10.7	-10.4	0.3	-9.0	1.6
	LSE	-1.9	-15.0	-13.4	-19.8	-11.3	-9.0	-4.3	4.7	-2.4	7.9

Source: KfW Research, ifo Institute

Explanations and abbreviations:

*Seasonally and mean adjusted (long-term mean since January 2005 = 0)

S(mall and) M(edium-sized) E(nterprises).

L(arge-)Scale E(nterprises).

Change in percentage points m(onth)-o(ver)-m(onth).

Change in percentage points y(ear)-o(ver)-y(ear).

Change in percentage points 3 m(onths period)-o(ver)-3 m(onths period).

Revisions relative to previous publications may occur due to seasonal and mean adjustments as well as rounding. The KfW-ifo SME Barometer was fundamentally revised for the reporting month of April 2018 (new aggregation process, inclusion of services, start of time series now 2005 instead of 1991, consideration of export expectations, discontinuation of regional indicators for western and eastern Germany). Publications prior to and from April 2018 are therefore comparable to a limited extent only.

Construction and interpretation of the KfW-ifo SME Barometer

The KfW-ifo SME Barometer indicator family is based on a scale-of-enterprise evaluation of the ifo economic surveys which are used to calculate, among other things, the well-known ifo Business Climate Index. Each month about 9,000 enterprises from trade and industry, construction, wholesale, retail and services (without the banking and insurance sectors or the state) are polled on their business situation, among them some 7,500 SMEs. Enterprises are generally classed as small to medium-sized if they employ a workforce of not more than 500 and record an annual turnover not exceeding EUR 50 million. For a more accurate analysis, however, these quantitative distinctions have to be drawn more narrowly for retail trade (maximum annual turnover of EUR 12.5 million), the building and the construction industry (up to 200 employees) and services (maximum annual turnover of EUR 25 million). All enterprises that exceed at least one of these thresholds are classed as large-scale enterprises. The KfW-ifo SME Barometer reports the balance of current business assessments (percentage of positive answers less percentage of negative answers), the balance of business expectations for the next six months, ascertained in a similar way, and the inferred mean average value for the business climate. Moreover, the enterprises' employment and domestic sales price expectations and – exclusively for manufacturing – export expectations are also captured as balance figures for the next three months. All time series are seasonally and mean adjusted. The zero line therefore marks the long-term 'cycle-neutral' average since January 2005. Indicators above (or below) zero point to an above average or favourable (below average or negative) business situation.